In the Supreme Court of the United States.

OCTOBER TERM, 1925

No. 29

THE UNITED STATES, *Appellant*,

vs.

BOSTON INSURANCE COMPANY

PETITION FOR REHEARING

A. R. SERVEN,
Counsel for Appellee.

JOHN G. CARTER, and
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Of Counsel.

PRESS OF GIBSON BROS., INC., WASHINGTON, D. C.

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To the Honorable, The Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner, the Boston Insurance Company, by its counsel, respectfully prays the rehearing and reconsideration of the above entitled cause for the following reasons:

By its opinion in this case, the Court reaffirmed the doctrine laid down by it in McCoach v. Insurance Company of North American (244 U. S. 585) and followed it here.

The opinion in the McCoach case seems to turn upon the fact that no statute of the State of Pennsylvania was found under which the Commissioner of Insurance of that State

was authorized to require fire and marine insurance companies to maintain policy loss reserve funds, and the further fact that the highest court of that State had not found the Commissioner clothed with authority to require such reserves. It was therefore held that the Commissioner's requirement of stock fire and marine insurance companies to hold policy loss reserves amounted to an improper administrative interpretation of the Pennsylvania Insurance Law.

The Court found that "The Pennsylvania Act specifically requires debts and claims of all kinds to be included in the statement of liabilities, and treats them as something distinct from reserves. The object is to exercise abundant caution to maintain the companies in a secure financial position." It therefore appears that in regard to debts and claims of all kinds, not including unearned premiums, the Commissioner was authorized to consider them in connection with solvency only. Consequently, reserves for these items did not come within the provisions of the Act of Congress providing for the deduction from gross income of "the net addition, if any, required by law to be made within the year to reserve funds." (36 Stat. L. 112.)

There are many analogous and also radically different provisions in the New York and Pennsylvania insurance statutes. It should be noted, however, that the analogous provisions relate to the ordinary and naturally inherent powers and duties of the department of a state government charged with the administration of its insurance laws. It should be further noted that the provisions in regard to annual statements and the examination of such companies, in order to determine whether the information contained in such statements is corroborated by the books, records, and papers of such companies, and also the computations in connection therewith, are all of a routine or so-called mechanical character, and are required by the ordinary supervisory

authority of such departments. However, these analogies are irrelevant and immaterial in the case at bar, where the first question relates solely to the reserve requirements of New York and Pennsylvania under their respective insurance laws, and the second question is whether these reserve requirements, or either of them, come within the meaning of the words "required by law" as used in the Revenue Act of 1916.

Section 7 of the Pennsylvania Public Laws, 607, approved June 1, 1911, in regard to unearned premium reserve for stock fire and marine insurance companies is as follows:

> "In determining the liabilities upon its contracts of insurance of any insurance company other than life insurance, and the amount such company should hold as a reserve for reinsurance, * * *. For fire insurance companies he shall charge fifty per centum of the premiums written in their policies upon all unexpired risks that have one year, or less than one year, to run, and a pro rata of all premiums on risks having more than one year to run; on perpetual policies he shall charge the deposit received, less a surrender charge of not exceeding ten per centum thereof. For marine and inland risks he shall charge fifty per centum of the premium written in the policy upon yearly risks, and the full amount of the premium written in the policy upon all other marine and inland risks not terminated."

This Court held in McCoach v. Insurance Company of North America, supra, that under the insurance laws of Pennsylvania, no other reserves were required to be held by such companies. The provisions of the New York Insurance Law, under which reserves are required to be maintained by fire insurance companies doing business in that State, are totally different. (Parker's New York Insurance Law, 1916, being Chapter 28 of the Consolidated Laws and

Chapter 33 of the New York Laws of 1909, and all amendments thereto.)

By Section 9, all corporations and individuals are prohibited from carrying on the business of insurance, as principals, in that State without first having secured the Superintendent's certificate authorizing them to do so. (Finding VII, R. p. 6.) By this section, the Superintendent is authorized to refuse his certificate of authority "if, in his judgment, such refusal will best promote the interests of the people of the State."

By Section 32, he is authorized to renew such certificate only "If the superintendent is satisfied that the capital, securities and investments remain secure, and that it may be safely intrusted with a continuance of its authority to do business." (Finding VII, R. p. 7.) By the same section he is also authorized as follows:

> "Whenever in the judgment of the superintendent of insurance it will best promote the interests of the people of this state, he may, after a hearing on notice, revoke the certificate of authority of a foreign corporation to do business in this state, prior to its expiration under this section."

It is under these provisions of Sections 9 and 32, and other concurrent sections, that the Superintendent of Insurance, in the exercise of his discretion therein granted, has required stock fire insurance companies to maintain the reserve funds enumerated in Finding VIII (R. p. 9), as a condition precedent to the transaction of business in the State of New York. That his reserve requirements under these sections are required by the New York Insurance Law is clearly demonstrated by other sections of that law. The second paragraph of Section 22, applicable to the unearned premium reserve of stock fire insurance companies, provides in part as follows:

"When a reinsurance agreement is made between other than life insurance corporations, the parties to such agreement shall, upon the policies involved, compute their unearned premium funds as follows: The reinsuring or ceding corporation shall, upon the portion of its liability not reinsured maintain a reserve to be computed in accordance with Section 118 of the insurance law; the corporation assuming liability by reinsurance from the corporation issuing the original policy shall maintain a reserve equal to that which the reinsuring corporation would have been required to maintain upon the amount reinsured had it retained the liability ceded by it."

It is the evident intent of this section to apportion the previously required unearned premium reserve between the ceding and reinsuring companies.

The last quoted clause clearly recognizes the legal requirement of a fire insurance company to maintain unearned premium reserves, to be computed as required by Section 118 (Findings VII, R. pp. 8-9), which relates solely to fire insurance companies. It should be noted here that Section 118 does not contain a requirement for the maintenance of unearned premium reserves, but treats unearned premiums solely as one of the liabilities of a fire insurance company. The provision of Section 118 referred to by Section 22 is as follows:

"In estimating its liabilities, there shall be charged, in addition to the capital stock and all outstanding claims, a sum equal to the total unearned premiums on the policies in force, calculated on the gross sum without any deduction on any account, charged to the policyholder on each respective risk from the date of the issue of the policy."

Section 47 provides as follows:

"No insurance corporation doing business in this state, or agent thereof, shall state or represent by advertisement in any newspaper, periodical or magazine, or by any sign, circular, card, policy of insurance or certificate of renewal thereof or otherwise, that any funds or assets are in possession of any such corporation not actually possessed by it and available for the payment of losses and claims, and held for the protection of its policyholders or creditors."

The first paragraph of Section 48 provides as follows:

"Every advertisement or public announcement, and every sign, circular or card issued by any insurance corporation or association incorporated by or existing under the laws of this state or of any other state of the United States and doing business in this state purporting to make known its financial standing, shall exhibit the amount of the capital actually paid in in cash, the assets owned, the liabilities, including therein the premium and loss reserves required by law, and the amount of net surplus of assets over all its liabilities actually available for the payment of its losses and claims, and held for the protection of its policyholders, and shall correspond with the verified statement made by it to the insurance department next preceding the making or issuing of the same. Every advertisement or public announcement, and every sign, circular or card issued by any insurance corporation or association incorporated by or existing under the government or laws of a country outside of the United States and doing business in this state, purporting to make known its financial standing, shall exhibit as capital and as assets only the capital and assets held by its United States branch, the liabilities, including therein the premium and loss reserves required by law, and the amount of net surplus of assets over all its liabilities actually available for the payment of its losses and claims and held for the protection of its policyholders in the United States, and shall correspond with the verified statement made

by it to the insurance department next preceding the making or issuing of the same."

That the issuance of the Superintendent's certificate of authority to transact business under Section 9 and its renewal under Section 32 involves more than mere solvency is clearly shown by Section 2 of Chapter 593 of the New York Laws of 1873, which is the original legislation bestowing discretionary authority upon the Superintendent in regard to his certificate of authority, as now contained in Sections 9 and 32. This section reads as follows:

> "The said superintendent shall have power to refuse admission to any company, corporation or association applying to be permitted to transact the business of insurance in this state from any other state or country whenever upon examination the capital stock of such company, corporation or association shall be impaired, and also whenever in his judgment such refusal to admit shall best promote the interests of the people of this state."

It will be noted that he is authorized by this section to refuse his certificate, first, whenever he finds that the capital stock is impaired, which involves the question of solvency, and, second, whenever he determines for any other cause that such refusal will best promote the interests of the people of the State.

In this connection, attention is also invited to the third paragraph of Section 33, in regard to his certificate of authority, which reads as follows:

> "Whenever it shall appear to the superintendent of insurance that permission to transact business within any state of the United States or within any foreign country is refused to a company organized under the

laws of this state, after a certificate of the solvency and good management of such company has been issued to it by the said superintendent and after such company has complied with any reasonable laws of such state or foreign country requiring deposits of money or securities with the government of such state or country, then and in every such case, the superintendent may forthwith cancel the authority of every company organized under the laws of such state or foreign government, and licensed to do business in this state, and may refuse a certificate of authority to every such company thereafter applying to him for authority to do business in this state, until his certificate shall have been duly recognized by the government of such state or country."

It must certainly be conceded that the Superintendent's requirement for unearned premium and loss reserves as a condition to issuing his certificate of authority is entirely in accord with the principles of good management and well adapted to protect and safeguard the interests of the policyholders. It must also be admitted that the exercise of his judgment in making such reserve requirements is equally well calculated to accomplish the purpose of the legislature in conferring such authority upon him, namely, "to best promote the interests of the people of the state." It should be further noted that the maintenance of these reserves by fire insurance companies, as required by the Superintendent, are most potent factors in determining whether companies may be safely intrusted with a continuance of their authority to do business. In fact, if these reserves were not required, in order to adequately safeguard and protect the interests of the policyholders, the Superintendent would be remiss in his duty to so exercise his judgment as "to best promote the interests of the people of the state."

The Pennsylvania Insurance Law is entirely lacking in

any provisions even remotely investing the Commissioner of Insurance with such authority in regard to the withholding, revoking, or refusing the renewal of certificates of authority to transact business in that State.

Nowhere in the Pennsylvania Insurance Law is there any mention of regulations of its insurance department, nor any suggestion, direct or remote, that the Pennsylvania Commissioner of Insurance was empowered to make regulations for the administration of the insurance laws of that State. In fact, a careful reading of the Pennsylvania laws would seem to justify the conclusion that the General Assembly intended by specific statutes to provide for all the necessary details of administration which are usually left to be provided for by departmental regulations.

The case is quite different, however, in regard to the New York Insurance Law. It would appear from the many grants of discretionary authority to the Superintendent, and the provisions expressed in general language, rather than in detail in other sections of the law, that the legislature intended to confer upon its insurance department ample authority to prepare and enforce all such regulations as might seem necessary and proper to supplement the statutory provisions. That this presumption in regard to the legislative intent is correct may be deduced from the further fact that although the New York statutes contain no express authority for such regulations, it refers to the regulations of the insurance department in Sections 25 and 27. The first paragraph of Section 25 is as follows:

> "The superintendent of insurance shall have the same supervision and make the same examination of the business and affairs of every foreign insurance corporation doing business in this state, as of domestic insurance corporations, doing the same kind of business, and of its assets, books, accounts and general

condition. Every such foreign corporation and its agents and officers shall always be subject to and be required to make the same statements and answer the same inquiries and be subject to the same examinations, and, in case of default therein, to the same penalties and liabilities as domestic insurance corporations doing the same kind of business, or any of the agents or officers thereof, are or may be liable to under the laws of this state or the regulations of the insurance department."

This provision seems to invest the regulations of the insurance department with the same force and effect as the statutes themselves, in regard to all matters coming within the supervision and regulation of the business of insurance in New York State.

In Section 27, relating to the funds and capital of insurance companies incorporated outside of the United States, the authority of the State insurance department to make and enforce regulations is also fully recognized. The second paragraph of this section provides as follows:

"The capital of such foreign fire insurance corporation, doing fire insurance business in this state, or of any such company hereafter admitted to such business in this state, shall, for the purposes of this chapter, be the aggregate value of such sums or securities as such corporation shall have on deposit in the insurance department of this state, and of the other states of the United States, for the benefit of policyholders in any of such states or in the United States, and of all bonds and mortgages for money loaned on real estate in this state or in any state of the United States, if such loans shall be made in conformity with the laws of such state providing for the incorporation of insurance companies therein and the investment of their capital, and of all other assets and property in the United States, in which fire insurance companies may invest under the provi-

sions of sections thirteen and sixteen, if such bonds and mortgages, assets and property shall be held in the United States by trustees, approved by the superintendent of insurance and citizens of the United States, or deposited with a trust company to be approved by him, for the general benefit and security of all its policyholders in the United States after taking from such aggregate value the same deductions for losses, debts and liabilities in this and the other states of the United States, and for premiums upon risks therein not yet expired, as is authorized or required by the laws of this state, or the regulations of its insurance department with respect to fire insurance companies organized under the laws of this state."

Under the provisions of this section, it would appear that the reserve requirements provided for by the rules, regulations and orders of the State insurance department are to be given the same authority in connection with fire insurance companies incorporated outside of the United States as if such reserve requirements were expressly provided for in the statutes themselves.

When the provisions of these two sections are considered in connection with the provisions of the various sections already referred to, and especially Sections 9 and 32, prohibiting the transaction of business in New York without the Superintendent's certificate, and prescribing the general conditions under which it might be granted, refused, renewed or revoked, it would appear to be the plain and obvious intent of the legislature that the Superintendent of Insurance should make all needful and proper regulations for enforcing such requirements as, in his judgment, were best adapted to fully protect policyholders and best promote the interests of the people of the State, and that such regulations should have the full force and effect of law. It is the general understanding that reserve funds are required for

the protection of policyholders, but under the provisions of the New York Insurance Law, the Superintendent of Insurance is required to go farther than this and to take such action as, in his judgment, will "best promote the interests of the people of the state." This provision seems to mean that he must take such action as will best promote the interests not only of the policyholders, but also of all of the people of the State. It is because of this provision of the New York Insurance Law, and other concurrent provisions thereof, that the Superintendent of Insurance has required not only unearned premium and policy loss reserves, in order to adequately protect the policyholders, but also reserves for all other liabilities of stock fire insurance companies, in order that such reserves might thereby become trust funds and therefore not subject to be dissipated for other purposes. (Reports of the Attorney General of New York, 1906, page 558.) This seems to have been the intent of the legislature in using the phrase in Section 9 "if, in his judgment, such refusal will best promote the interests of the people of the state," and similar phrases in other sections of the insurance law. This intent seems also to be supported by the legislature's recent amendment of Section 117, in regard to the computation of the funds of an insurance company available for the purpose of paying dividends. The first paragraph of this Section reads as follows:

> "Estimation of Surplus. In estimating surplus of a fire insurance corporation for the purpose of making any dividend upon its capital stock, there shall be reserved from its admitted assets, a sum equal to the amount of all unearned premiums on unexpired risks and policies, and all outstanding liabilities. But no corporation may declare dividends exceeding ten per centum on its capital stock in any one year unless, in addition to the amount of its capital stock, such dividend, all outstanding liabilities and the amount of all

unearned premiums on unexpired risks and policies as aforesaid, it shall have and be in possession of a surplus to an amount equalling thirty per centum of its unearned premiums or fifty per centum of its capital stock, whichever shall be greater." (Parker's, 1923.)

The regulations of the New York Insurance Department should not, therefore, be regarded as mere administrative interpretations of the law, as the Court held was the case in McCoach v. Insurance Company of North America, supra, in regard to the Pennsylvania Insurance Commissioner's requirement of policy loss reserves, but must be given the full force and effect of duly authorized departmental regulations, in pursuance of appropriate authority of law. This is especially true because the highest court of New York has affirmed the authority of the Superintendent of Insurance in the exercise of his discretion in connection with his certificates of authority to transact business in that State. (See People ex rel. Hartford L. & A. Insurance Co. v. Fairman, 91 New York 385, and People ex rel. Equitable F. & M. Insurance Co. v. Fairman, 92 New York 656.) This is also in accordance with a long line of decisions of this Court sustaining the integrity and validity of such regulations, both Federal and State, and giving to them the same force and effect they would have had if actually written into the statutes.

As policy loss reserves have been required by the Superintendent of Insurance since about 1874, as shown by his certificate attached hereto and made a part hereof, it would appear, according to many decisions of this Court that when the legislature re-enacted in Section 9 of the present insurance law the provisions of Section 2 of the Act of 1873, as quoted above, it thereby adopted the Superintendent's construction of the language so re-enacted and made his requirement for the maintenance of these reserves a require-

ment of law as fully as if the legislature had written it into the body of the re-enacted statute.

It would appear that the language of the above quoted provisions of the New York Insurance Law fully justify the conclusion that it was the plain and obvious intention of the legislature that the Superintendent of Insurance should make such requirements of appellee, and other similar insurance companies, as would adequately protect the interests of their policyholders, and that in pursuance of this intention he was invested with full authority to do so. In accordance with this authority, the Superintendent has required such companies to maintain loss claims reserves continuously since about 1874 and his exercise of this authority has apparently had the full approval of the legislature, as shown by the fact that it has never in any way withdrawn or modified such authority. But even had the Superintendent's reserve requirements not been matured into departmental regulations, with full recognition in the statutes and possessing the full force and effect of law, nevertheless this long continued interpretation of the insurance department in requiring these reserves would be entitled to the greatest consideration, even as a mere administrative interpretation. However, it has been held that long continued departmental usage and practice may constitute a regulation, even if never reduced to writing. Perhaps the authority for this usage and practice may rest in the incidental powers to be implied from the legislation under which such usage and practice has arisen.

The Court's opinion in this case seems to suggest that a State statute duly enacted, and not repugnant to the Constitution, with appropriate regulations in pursuance thereof by the executive department charged with the administration of such statute, are not necessarily sufficient to satisfy the requirement of law within the meaning of the income tax

act of 1916. The words "required by law" in this act should be given their usual and ordinary meaning as generally understood. It would appear that Congress intended by the use of these words to provide that increases which were required under any lawful authority to be made to reserve funds of insurance companies should be deducted from gross income. In the case at bar we have the statutes of New York, supplemented by the appropriate regulations of its insurance department requiring these reserves, and, in addition thereto, Finding VI (R. p. 5) shows that in compliance with these requirements appellee held, set aside, and retained funds as reserves in the amount and on account of its liability for loss claims, while Finding X (R. p. 10) shows that such loss reserve funds were required to be set up specifically on appellee's books as the reserve to meet liabilities on account of unpaid loss claims.

In view of the full faith and credit clause of the Constitution, it would appear that the New York statutes and the regulations in pursuance thereof, and the compliance with such regulations by appellee, should be sufficient to fully satisfy the expression "required by law" as used in the tax act. It would seem that Congress by these words intended to mean in pursuance of State statutes, as it has been so frequently held by this Court that the States had reserved to themselves full power and authority to legislate on all matters concerning the business of insurance.

Under these circumstances, in view of the repeated enactments now crystallized into sections 9, 32, 33, 39, 47, 48, 54, 66, 138a, 143, 159, and many others of the New York Insurance Law, of the purpose of the New York legislature to provide ample and adequate protection for the interests of the policyholders and the people of that state, it would seem that the Court might be justified in holding that a failure to require both unearned premium and

policy loss reserves in New York State would amount to a serious breach of public policy.

The certificate of the Superintendent of Insurance, hereto attached and made a part hereof, makes it clear that the unearned premium reserve is not sufficient to adequately protect the interests of the policyholders and, therefore, the loss claims reserve has been found necessary in order to carry out the intent of the legislature that the interests of the policyholders should be adequately safeguarded and protected.

In the light of this certificate and the provisions of the New York Insurance Law hereinbefore referred to, the application to the case at bar of the doctrine of McCoach v. Insurance Company of North America would seem to be entirely inappropriate, as it in no way constitutes a construction of the pertinent sections of the New York Insurance Law.

Wherefore, the premises considered, your petitioner prays that this cause may be reopened and reconsidered and such further action taken therein as to the Court may seem just and proper.

A. R. SERVEN,
Counsel for Appellee.

JOHN G. CARTER, and
JOHN W. SMITH,
Of Counsel.

A. R. SERVEN being duly sworn deposes and says that he is counsel for the appellee in the above-entitled cause and has read the foregoing petition for rehearing and knows the contents thereof, and that the same are true to the best of his knowledge and belief, and that the said petition is not presented for purpose of delay.

A. R. SERVEN.

Subscribed and sworn to before me this 31st day of December, A. D. 1925.

W. B. JAYNES,
Notary Public, D. C.

(SEAL)

STATE OF NEW YORK

INSURANCE DEPARTMENT

ALBANY

JAMES A. BEHA,
Superintendent of Insurance.

I, JAMES A. BEHA, Superintendent of Insurance, do hereby certify that under authority of Section 2, Chapter 593, of the 1873 laws of New York, approved May 22, 1873, as superseded or amended by Section 9 of the present insurance law, Section 2 of Chapter 888 of the 1871 laws of New York, as superseded or amended by Section 27, of the present insurance law, Chapter 725 of the 1893 laws of New York, as superseded or amended by Section 32 of the present insurance law and other New York laws and amendments thereto relating to the subject of insurance, and the rules, regulations and orders of the New York State Insurance Department issued in pursuance thereof, since the enactment of such laws (or about 1874) all stock fire and marine insurance companies transacting business in this State have been required to maintain loss claim reserve funds sufficient to protect all unpaid policy losses at the end of each respective year, the purpose of this requirement being to provide reserves as security for the payment of such losses, as the unearned premium reserve also required under the statutes, rules, regulations and orders above referred to does not provide security for the settlement of such unpaid loss claims. The unearned premium reserve is intended to provide for the payment of reinsurance and return premiums but not for the payment of loss claims arising under the policies for which the unearned premium reserve is maintained. The unearned premium reserve is recomputed periodically either monthly or more generally annually, the premiums earned being deducted from the

unearned premium reserve, such earned premiums automatically flowing into the company's surplus out of which in turn automatically flow sums required to be set up as loss reserves for the payment of losses. The purpose of the Insurance Department in requiring loss claim reserve funds in addition to unearned premium reserves is well known to all fire and marine insurance companies transacting business in this State as well as to insurance supervising officials and to others who are generally interested in this matter.

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the official seal of this Department, at the City of Albany, this 28th day of December, 1925.

JAMES A. BEHA,

[SEAL] *Superintendent of Insurance.*